MEMORANDUM

October 14, 1974

TO: The Honorable Dean Burch,
Counsellor to the President

FROM: Ray Garrett, Jr., Chairman
Securities and Exchange Commission

RE: Possible Topics for Discussion at Conference with the President at 12:15 p.m., October 14, 1974

Pursuant to the request of your staff, I have set forth three areas that the President may wish to discuss at our conference.

Budget, Appointments, etc. The Securities and Exchange Commission has no current problems in this area that need be of concern to the President. The next Commissioner's term of office to expire -- we have staggered five-year terms -- is that of Irving M. Pollack, Democrat, on June 5, 1975. I am very eager to see Mr. Pollack reappointed, but that does not require immediate attention.

Legislation. After the election, and before Christmas, we expect the Congress to approve comprehensive legislation affecting the securities markets and the Securities and Exchange Commission's authority and responsibility. This is the most comprehensive piece of legislation relating to securities market regulation since the creation of the Securities and Exchange Commission in 1934. The Secretary of the Treasury and the President's Congressional Liaison Staff, as well as the Securities and Exchange Commission, successfully urged favorable action by Congressman Staggers' Committee on Interstate and Foreign Commerce on H.R. 5050, the House counterpart to several bills already adopted by the Senate. Assuming no surprise in what comes out of conference, we expect to recommend that the President sign this legislation.

Other related legislation has been submitted, but we do not expect any action on them by this Congress.

Securities Markets. It is well known that our markets for stocks and bonds have been in a prolonged, declining trend. The declining trend appears to be part of a world-wide phenomenon, generally thought to be closely related to inflation. One result has been great difficulty for the securities industry -- the broker-dealer and investment banking firms -- to raise capital from the public for corporate expansion.

This subject was aired at the Pre-Summit Conference on Banking and Finance. Last week we saw an upsurge in stock prices and trading volume on the New York Stock Exchange, but it is impossible to tell whether this indicates a long-range favorable trend.

It is not so well recognized that the securities industry has been suffering severely. Attached, for your information, is a copy of one of our two submissions to the Pre-Summit Conference on Banking and Finance.

Aside from certain tax proposals to strengthen securities firms in the future, the foreseeable problem likely to concern the President in the coming year is the relationship of commercial banks and bank holding companies to the securities industry. Some, though apparently not all, of the major bank holding company systems are pressing for the legal right to become more directly engaged in the securities business through permissive rules which they seek to have adopted by the Board of Governors of the Federal Reserve System or through relaxing amendments to the Glass-Steagall Act.

The problem is not only what is good for banks. Direct bank competiton could be so devastating to existing securities firms that the problem is also whether we wish to preserve an independent securities industry, meaning one not dominated by banks and bank holding companies. Without such an independent securities industry, the freedom of access of companies to the public capital market might be curtailed.

Attachment

OFFICE OF THE CHAIRMAN

# SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

## STATEMENT OF CHAIRMAN RAY GARRETT, JR. REGARDING "CAPITAL MARKETS AND CAPITAL FORMATION"

Ensuring the availability of adequate long term capital over the next decade is clearly one of the most necessary requirements for this country's future economic growth. However, in addition to measures designed to make capital available for investment and to make investment attractive, we must be certain that the mechanism for raising equity and long-term debt is not destroyed by the disappearance of a high capacity, diversified, securities industry.

The securities industry is in an alarming downward trend. New York Stock Exchange member firms, which account for approximately 75 percent of the revenues of the industry, lost $66 million before tax in 1973 and have reported a $49 million loss for this first half of 1974. The profit problem is widespread: in eleven of the last twenty-four months, 50 percent or more of the New York Stock Exchange firms have reported losses. And between 1971 and 1973 the number of New York Stock Exchange carrying public customer accounts declined 16 percent. Further, it does not appear that the industry is simply suffering through the low point in this profitability cycle, offsetting the high point in the late1960's. Our preliminary data indicate that the return on equity in the industry currently is well below that experienced at the bottom of the previous cycle and about one-tenth of the median rate of the past seven years.

An upward trend in prices and volume will benefit the securities industry, but there are other adverse trends that need examination. I recommend that interested government agencies conduct a coordinated review of the respective role of, and government policies toward, our many different financial institutions considering both existing statutes and future requirements with respect to the process of capital formation for American industry. As one example, securities industry has expressed deep concern that the aggressive expansion of banks and bank holding companies into new services in recent years while the securities industry has been declining, has created an unequal competitor for the securities industry, both because of the size of the banks and because they appear to be regulated by agencies whose primary concern is the health of the banking system. If we are to preserve a healthy securities industry independent of domination by commercial banks, protective measures may be indicated.